Canadian Radio-television and Telecommunications Commission
Conseil de la radiodiffusion et des télécommunications canadiennes

Telecom Decision CRTC 2005-4

Ottawa, 31 January 2005

Implementation of competition in the local exchange and local payphone markets in the territories of Société en commandite Télébec and the former TELUS Communications (Québec) Inc.

Reference: 8622-C12-14/01

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In this Decision, the Commission determines that the banding structure adopted for the large incumbent local exchange carriers (ILECs) will be adopted in the territories of Société en commandite Télébec (Télébec) and the former TELUS Communications (Québec) Inc. (TELUS Québec).[1]

The Commission establishes the unbundled local loop and the residential primary exchange service (PES) costs for Télébec and TELUS Québec, for the purpose of determining unbundled loop rates and subsidy calculations, respectively.

The Commission ***approves*** *the Type A unbundled local loop rates for Télébec and TELUS Québec, based on the Phase II costs determined in this Decision plus a 25 percent mark-up.*

The Commission also establishes the rates for other local interconnection services, including local payphone access. These other local interconnection service rates are to be set at either the rates already approved for Bell Canada, plus a multiplicative factor of 8.7 percent to reflect rates at Phase II costs plus 25 percent, or at the rates that are supported by ILEC-specific costs plus a 25 percent mark-up.

The Commission determines that subsidies will not be extended to business PES in high-cost serving areas within the territories of Télébec and TELUS Québec, and that the current quality of service standards remain in place for these companies.

Finally, the Commission ***approves, on a final basis****, the 2003 and 2004 subsidy requirements for Télébec and TELUS Québec, and issues directives to Télébec with respect to the reinstatement of basket constraints pursuant to price cap regulation.*

Introduction

1. In *Changes to the contribution regime*, Decision CRTC 2000-745, 30 November 2000 (Decision 2000-745), the Commission introduced a new subsidy requirement calculation, applicable to all telecommunications service providers, to ensure that the contribution regime provided an appropriate amount of subsidy to maintain affordable residential primary exchange service (PES) in high-cost serving areas (HCSAs).

2. In *Restructured bands, revised loop rates and related issues*, Decision CRTC 2001-238, 27 April 2001, as amended by Decision CRTC 2001-238-1, dated 28 May 2001 and Decision CRTC 2001-238-2, dated 7 August 2001 (Decision 2001-238), the Commission approved revised rates for the large incumbent local exchange carriers' (ILECs') unbundled local loops. The Decision also addressed the costs to be used for establishing the subsidy required for each ILEC under the national subsidy mechanism approved by the Commission in Decision 2000-745. In addition, the Commission adopted a uniform approach to identify HCSAs in the large ILECs' territories, and a more consistent set of costing methodologies by which the large ILECs would determine the costs for the unbundled local loops and residential PES.

[1] Following the close of this proceeding, the Commission was advised that, as of 1 July 2004, TELUS Québec ceased to operate as a Canadian carrier or telecommunications service provider and that TELUS Communications Inc. (TCI) assumed all rights, entitlements, liabilities, and obligations relating to the provision of telecommunications services in the territories previously serviced by TELUS Québec. For ease of reference, TELUS Québec is used throughout this Decision.

3. In *Implementation of price regulation for Télébec and TELUS Québec*, Telecom Decision CRTC 2002-43, 31 July 2002 (Decision 2002-43), the Commission established the price regulation regime now applicable to Société en commandite Télébec (Télébec) and TELUS Communications (Québec) Inc. (TELUS Québec)[2] (collectively, the Companies).

4. In *Implementation of competition in the local exchange and local payphone markets in the territories of Télébec and TELUS (Québec)*, Public Notice CRTC 2001-69, 14 June 2001 (Public Notice 2001-69), the Commission initiated a proceeding to establish the rates for local interconnection and unbundled network components, and local payphone access, in the Companies' territories. Issues that were to be addressed in the proceeding included:

- proposals concerning rate band structure, taking into account the need to identify HCSAs in their respective territories in view of the Commission's conclusions in Decision 2001-238, and the subsequent calculations of the per-line subsidy requirements based on the formula set out in Decision 2000-745 and using the current residential PES rates;

- proposed unbundled local loop and residential PES costs per band with supporting cost studies consistent with the methods prescribed in Decision 2001-238, or in the alternative, other costing methods with detailed explanations of the assumptions used and why those methods were required;

- proposed rates, with supporting cost studies, for the following services:

  i. unbundled local loops;

  ii. other local network components to be unbundled pursuant to *Local competition*, Telecom Decision CRTC 97-8, 1 May 1997 and *Final rates for unbundled local network components*, Telecom Decision CRTC 98-22, 30 November 1998, as amended by Telecom Decision CRTC 98-22-1, dated 10 December 1998 (Decision 98-22);

  iii. the delivery of traffic from one competitive local exchange carrier (CLEC) to a customer of the ILEC located within the same exchange (i.e., traffic imbalance service);

  iv. the delivery of traffic from one CLEC to a customer of the ILEC located in another exchange, but within the toll-free calling area of the originating exchange (i.e., extended area service [EAS] termination service);

  v. transit services, for traffic and for signalling (CLEC to CLEC, CLEC to wireless service providers [WSPs], and CLEC to long distance service providers); and

  vi. access lines to competitive pay telephone service providers (CPTSP), and an associated standard service agreement;

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[2] See footnote 1.

- proposed quality of service (Q of S) indicators; and

- the potential extension of subsidies to business PES in HCSAs.

5. The Commission received comments pursuant to Public Notice 2001-69 from Bell Canada; RTS Canada, on behalf of the Grand Council of the Crees and the James Bay Cree Communications Society (RTS); and Mr. François Ménard (Mr. Ménard).

6. In this Decision, the Commission first examines the Companies' proposed rate band structure and related issues. The Commission then assesses unbundled local loop and residential PES costing issues, including the establishment of the appropriate costs for residential PES and the rates for unbundled loops. The Commission then deals with the rate issues raised in Public Notice 2001-69, Q of S issues, and the question of whether subsidies should be extended to business PES in HCSAs. Finally, the Commission addresses the implementation issues associated with Public Notice 2001-69, including the Companies' subsidy requirements and the annual price cap commitments required pursuant to Decision 2002-43.

Rate band structure

7. In Decision 2000-745, the Commission introduced a uniform subsidy calculation for all ILECs, based on HCSAs. The Commission noted that HCSAs would be established based on a uniform banding structure and that the subsidy per residential network access service (NAS) in each HCSA would consist of Phase II costs per NAS, plus a 15 percent mark-up, less (the average residential local service rates plus an implicit subsidy amount associated with optional features).

8. In Decision 2001-238, the Commission approved the use of the uniform banding structure for the large ILECs, which included the following non-high-cost serving area (non-HCSA) bands:

- Band A, which generally included core exchanges of major urban centres;

- Band B, which generally included non-core exchanges of major urban centres and exchanges of other urban areas;

- Band C, which generally included exchanges with > 8,000 NAS; and

- Band D, which generally included smaller exchanges with >1,500 NAS and < 8,000 NAS and a local loop length of < 4 kilometres.

9. The Commission also approved the following HCSA bands:

- Band E, which included exchanges with < 1,500 NAS;

- Band F, which included exchanges with > 1,500 NAS and < 8,000 NAS and a local loop length of > 4 kilometres; and

- Band G, which was defined as the remote band (i.e., those wire centres or exchanges without year-round road access or found in remote parts of an ILEC's serving territory).

Positions of parties

10. Télébec proposed modifications to the banding structure developed in Decision 2001-238 such that all of its exchanges would be classified as HCSAs and eligible for subsidy funding pursuant to Decision 2000-745. Télébec submitted that the Commission had previously recognized that the definition of HCSAs could be adjusted in order to meet the specific characteristics of each ILEC.

11. Specifically, Télébec proposed the following banding structure:

- Band D included exchanges with > 8,000 NAS, and a local loop length of < 4 kilometres;
- Band E-1 included exchanges with < 1,500 NAS, and a local loop length of < 4 kilometres;
- Band E-2 included exchanges with < 1,500 NAS, and a local loop length of > 4 kilometres;
- Band F-1 included exchanges with > 1,500 NAS and < 8,000 NAS and a local loop length of < 4 kilometres;
- Band F-2 included exchanges with > 1,500 NAS and < 8,000 NAS and a local loop length of > 4 kilometres;
- Band F-3 included exchanges with > 8,000 NAS and a local loop length of > 4 kilometres; and
- Band G included remote exchanges.

12. Télébec indicated that, according to its proposed banding structure and costing, it did not have any exchanges that qualified as non-HCSAs (i.e., Bands A, B, C, or D as set out in Decision 2001-238).

13. Télébec indicated that the Commission's classification of HCSAs, in Decision 2001-238, significantly affected the subsidy that it could receive. Télébec argued that the characteristics of its territory resulted in higher costs to provide residential PES service and, as such, warranted support from the national fund to ensure that rates would be maintained at reasonable levels. Télébec argued that if the Commission did not identify all of its proposed bands as HCSAs, then Télébec would be offering its residential PES at a rate below cost. Télébec argued that it would be difficult for competitors to offer service in its territory if rates were not compensatory.

14. TELUS Québec proposed to classify its Bands C and D using criteria similar to those used to establish Bell Canada's Bands C and D. As such, TELUS Québec proposed that Band C include small exchanges with > 10,000 NAS, and Band D include small exchanges with < 10,000 NAS. TELUS Québec further proposed to classify its Bands E, F, and G consistent with the criteria established in Decision 2001-238.

15. With respect to its subsidy calculation, TELUS Québec proposed that the Band D NAS be considered eligible for subsidy funding, regardless of the length of the local loop. TELUS Québec also indicated that the Commission should consider extending the subsidy calculation to include Band C NAS with loop lengths in excess of 4 kilometres given the higher costs of serving these NAS. TELUS Québec argued that, based on its proposed residential PES costs in Band D, rates were not compensatory. TELUS Québec indicated that Decision 2002-43 did not provide the company with the flexibility to bring its residential PES rates closer to cost, and that therefore service in those exchanges should be subsidized.

16. In their reply comments, the Companies both argued that the historical structure of their respective networks had had a significant impact on their costs and would also impact their subsidy calculations. The Companies argued that the amount of subsidy that they received should not be hindered as a result of their historical network configurations.

17. TELUS Québec disagreed with Télébec's proposed banding structure. TELUS Québec indicated that if the Commission applied Télébec's proposed banding structure to TELUS Québec, the company would receive 60 percent more subsidy than it had proposed in its own submission.

18. For its part, Télébec disagreed with TELUS Québec's proposal to extend the subsidy calculation to include Band C NAS with loop lengths in excess of 4 kilometres. Télébec argued that treating certain NAS within the same exchange differently would be contrary to the Commission's determinations in Decision 2001-238. Télébec considered that TELUS Québec's proposal would be difficult to manage and would also create significant administrative problems.

Commission's analysis and determinations

Non-HCSA bands

19. With respect to Télébec's proposal, the Commission notes that while Télébec did not propose to classify any of its exchanges as non-HCSAs, the company's proposed Bands F-3 and F-1 displayed similar characteristics to those of Bands C and D, respectively, within the territories of TELUS Québec and other large ILECs.

20. The Commission notes that Télébec's proposed Band F-3 includes the Rouyn-Noranda and Val-d'Or exchanges, each of which serve a total number of NAS in excess of 17,000. The Commission notes that most of the large ILECs, including TELUS Québec, classified similar exchanges or wire centre serving areas into Band C. Similarly, the Commission notes that the criteria established for Télébec's proposed Band F-1 is equivalent to the criteria established for Band D of the other large ILECs.

21. The Commission notes that Télébec's residential PES costs in Bands F-3 and F-1, as adjusted to reflect the determinations in this Decision and expressed in 2002 dollars, are less than the corresponding residential monthly revenue per NAS. The Commission therefore finds that Télébec's proposed Bands F-3 and F-1 are to be classified as non-HCSA Bands C and D, respectively, and are not eligible for subsidy funding.

22. With respect to TELUS Québec's proposal to extend subsidies to Band C NAS having loop length in excess of 4 kilometres, the Commission considers that this would have the effect of creating a band-split based on subsets of NAS within the Band C wire centres or exchanges. The Commission considers that TELUS Québec's proposal relies on a banding structure that is narrower than the exchange or wire centre level, which is inconsistent with the banding structure adopted for the large ILECs in Decision 2001-238. The Commission notes that TELUS Québec's proposal would add significant administrative complexity to the banding structure. Further, TELUS Québec has not furnished any details to identify the NAS that would qualify under this proposal nor the Phase II costs by sub-band in support of its proposal. The Commission considers that TELUS Québec has not provided the necessary justification to support a deviation from the banding structure approved in Decision 2001-238. Therefore, the Commission finds it inappropriate to accept TELUS Québec's proposal to extend subsidies to Band C NAS having loop length in excess of 4 kilometres.

23. The Commission further notes that when the subsidy calculation established in Decision 2000-745 is applied to TELUS Québec's residential PES monthly revenue per NAS and costs in Bands C and D, as adjusted to reflect the determinations in this Decision and expressed in 2002 dollars, there is no subsidy requirement over the aggregate of these two bands. In light of this, the Commission finds that TELUS Québec's proposed Bands C and D are to be classified as non-HCSA bands and are not eligible for subsidy funding.

HCSA bands

24. The Commission notes that Télébec proposed to split Band E into two sub-bands - Bands E-1 and E-2.

25. The Commission considers that a band-split would be desirable if high demand was expected for the unbundled loop service in either band and the cost differential was sufficient to warrant such a band-split. The Commission notes that, based on Télébec's residential PES costs, as adjusted to reflect the costing determinations in this Decision, the cost differential between Bands E-1 and E-2 is only approximately 26 percent. The Commission notes, further, that it expects minimal competitor demand for unbundled local loops in these low-density HCSA bands.

26. The Commission is of the view that Télébec's proposed sub-banding is not necessary for subsidy calculation purposes, since the company would receive the same amount of subsidy (under the current subsidy formula) whether separate costs for Bands E-1 and E-2, or whether the average costs over the aggregate of Band E, are used.

27. In light of the above, the Commission finds that Télébec's proposed Bands E-1 and E-2 should be merged into one HCSA band, Band E, consistent with its determinations for the other large ILECs. Further, the Commission finds that Télébec's proposed Bands F-2 and G should be

classified as Bands F and G, respectively, as they are consistent with the Bands F and G as defined for the other large ILECs. The Commission also finds TELUS Québec's proposed classifications for Bands E, F, and G to be appropriate.

Costing of unbundled local loops and residential primary exchange service

28. In Public Notice 2001-69, the Commission required TELUS Québec and Télébec to apply the Decision 2001-238 costing parameters in developing their unbundled loop and residential PES cost studies unless they could provide the necessary justification to deviate from such determinations. The major determinations set out in Decision 2001-238 applicable to the large ILECs included the following: (a) use of a five-year study period; (b) use of accounting plant life estimates; (c) use of average working fill factors (AWFF) of 77 percent for feeder plant and 60 percent for distribution plant in non-HCSA bands, and 72 percent for feeder plant and 56 percent for distribution plant in HCSAs; (d) functional operating expense (FOE) caps of $1.65 per unbundled loop and $2.50 per residential PES; and (e) maintenance expense caps of 10 percent of capital for all bands except Band G, which was to be capped at $20 per NAS.

Positions of parties

29. Télébec indicated that it had concerns with respect to the reliability and transparency of Phase II costing, and submitted that Phase III costing was verifiable and, in its view, constituted a more reliable and logical base for its costs. Télébec indicated that, although Phase II costing was growing in importance with respect to local competition, the company considered it important to establish its Phase III costs in order to determine the actual costs of providing residential PES to its customers, compared to the costs that would be established using Phase II costing.

30. As such, Télébec calculated its Phase III costs by exchange. Next, Télébec designated a typical exchange for each of its seven proposed bands using Phase III costs, local loop length and the number of NAS in the exchange. Télébec then calculated the Phase II costs of the designated exchange for each band. Télébec indicated that, in order to adequately estimate the average Phase II costs within each band, it determined the per-band average costs from the designated exchange Phase II costs based on a comparison of the key cost characteristics between the band's designated exchange and the average of the exchanges within the band.

31. Télébec indicated that it did not have the resources to do Phase II costing for all of its exchanges, but submitted that the methods and assumptions used in its Phase II studies for its designated exchange within each band complied with those approved by the Commission.

32. Télébec argued that applying a common mark-up would penalize the company, since its operational costs per NAS were higher as a result of the unique nature of its territory. Télébec submitted that, based on its calculations, there was a significant difference between its costs using a Phase II versus a Phase III methodology. Télébec requested that the Commission allow the company to recover the difference between Phase III and Phase II costs by approving a specific mark-up factor to be applied to the company's Phase II costs, in each of its rate bands, in order to bring them to Phase III cost levels. Télébec submitted that since it considered all of its exchanges as HCSAs, the mark-up on Phase II costs used to determine the subsidy requirement was of high importance to the company.

33. Télébec argued that despite having among the highest residential PES rates in Canada, the deficit that it incurred to offer local service was significant. Télébec noted that, based on the costing study that it provided, none of its residential PES rates were compensatory, even in light of its higher rates. Télébec noted that it did not have the flexibility to raise rates for residential PES and indicated that if it was to continue to offer quality service at reasonable rates, it needed subsidy support to recover all the costs of its service. Télébec submitted that it should be able to recuperate, through either rates or subsidy, all of its actual and past investments made in order to offer local service.

34. Télébec noted that its outside plant network costs (consisting mostly of copper cable and support structures) were high relative to its total network costs as a result of its serving territory that was characterized by long local loops and a low population density. Télébec argued that large ILECs serve a greater proportion of urban centres and that applying national AWFF averages, rather than the company's actual fill measures, resulted in expenses that would neither be recognized nor compensated. Télébec argued that, for a company serving mainly remote areas, the negative impact of excluding these costs would be accentuated compared to the large ILECs that serve a greater proportion of urban centres. In response to a Commission interrogatory, Télébec explained that only its rapid-growth sectors could be expected to reach the national AWFFs prescribed by the Commission in Decision 2001-238.

35. TELUS Québec indicated that in contrast to the other ILECs' local networks that relied on feeder and distribution plant network configurations, its local network consisted almost entirely of distribution plant. TELUS Québec submitted that its AWFF for its copper cable was 59 percent, and that it did not consider it appropriate to apply the national AWFF averages since these were developed based on the other ILECs' networks.

36. TELUS Québec also argued that the Commission should not use the AWFF cost sensitivity results associated with the use of minimum cable sizes of 25-pair or 50-pair cables, since such sensitivity results did not correspond with the characteristics of its territory or the network that would be required in the event that it were replaced.

37. TELUS Québec submitted that it did not use the Commission-prescribed ratios in the establishment of its FOE and maintenance costs, but instead relied on its actual costs. TELUS Québec argued that it did not benefit from the same economies of scale as the large ILECs in light of its largely rural territory.

38. TELUS Québec indicated that it prepared its cost studies using replacement costs for the network that was currently in place, which represented a smaller capacity than those attained by the large ILECs. TELUS Québec argued that this was economically sound since there were regions in its territory where growth would be almost zero or negative.

39. In its reply comments, TELUS Québec noted that Télébec's proposal to use its Phase III costs would prolong the use of that model, whereas Decision 2002-43 stipulated that the Phase III costing methodology was no longer required for the Companies. TELUS Québec argued that it would no longer be appropriate to use Phase III costing and that it would be preferable for the Commission to require that Télébec use Phase II costing, consistent with the other large ILECs.

40. TELUS Québec did agree with Télébec, however, that the uniform mark-up of 15 percent imposed on the large ILECs in Decision 2001-238 would not provide the Companies with the ability to ensure that their rates would be compensatory. TELUS Québec argued that a 15 percent mark-up on residential PES was contrary to the Commission's objective to ensure that competition and efficiency were allowed to develop, and provided no motivation for competitors to enter the local service market, particularly in remote areas.

41. Télébec agreed with TELUS Québec's position that it would be inappropriate to use the national AWFF averages set out in Decision 2001-238 for the Companies.

42. In reply to TELUS Québec's concerns regarding the costing methodology used, Télébec indicated that it had developed Phase II costs for the designated exchanges as adjusted to reflect the band-average Phase II costs. Télébec submitted, however, that it underwent an exhaustive study of its entire network in order to establish Phase III costs at the detailed exchange level in order to permit a comparison of its Phase II costs with its actual audited Phase III cost results. Télébec stated that its intent was not to prolong the use of Phase III costing, but to present, with as much precision as possible, its actual costs of delivering residential PES. Télébec also considered that this methodology would help the Commission appreciate the costs that were not recognized, or compensated for, by the Phase II costing methodology.

Commission's analysis and determinations

Télébec's mark-up proposal to recognize embedded costs for subsidy purposes

43. The Commission notes Télébec's position that it should be entitled to recover through its rates or subsidy all of its actual and past investments in order to offer local service. For purposes of determining its subsidy requirement, Télébec proposed to apply a variable mark-up designed to recover the differences between Phase III embedded costs and Phase II current costs for each band.

44. The Commission also notes that Télébec's request to recover past or embedded costs was previously rejected in Decision 2000-745. In that Decision, the Commission indicated, among other things, that: (a) the Phase III-based costing approach would not allow for the identification of costs in HCSAs; (b) the forward-looking incremental Phase II costs of providing residential PES would deliver the appropriate incentives for efficient provision of service and competitive entry in HCSAs; (c) a mark-up of 15 percent on the Phase II costs of residential PES would provide a sufficient level of contribution towards the ILECs' fixed and common costs; and (d) this mark-up level would not consider the differences between Phase III embedded costs and Phase II current costs.

45. The Commission considers that to grant Télébec's request to recognize more than the Phase II costs and a 15 percent mark-up, for subsidy calculation purposes, would be contrary to the determinations in Decision 2000-745. The Commission further considers that Télébec did not make a compelling case to demonstrate why the principles of Decision 2000-745 should not be applied to it.

46. Accordingly, the Commission **denies** Télébec's request to consider amounts other than Phase II costs plus a 15 percent mark-up for the purpose of determining the subsidy requirement.

General costing assumptions

47. The Commission notes that TELUS Québec and Télébec developed their unbundled loop and residential PES Phase II cost studies by generally applying the Decision 2001-238 determinations, such as using a five-year study period, the approved accounting plant lives, and the FOE caps. The Commission notes, however, that the Companies deviated from the Decision 2001-238 costing determinations in certain aspects, such as the AWFFs and maintenance expenses. In its analysis of the costing evidence, the Commission also uncovered certain costing inconsistencies or irregularities. The various costing issues are discussed below.

AWFFs

48. The Commission notes that the AWFF measure is used as an input in the capacity cost formula. AWFFs are applied to the capacity cost estimates for the various shared plant resources to recognize the spare capacity of plant in Phase II cost studies, by apportioning the average non-service producing capacity to the per-unit cost of the service producing capacity.

49. Under this approach, the AWFF used to determine the capacity cost estimate should reflect the appropriate economic forward-looking average working fill measure over the study period. The Commission notes that the spare capacity that is implicit to the use of average working fill may be disallowed for causal costing purposes if it is viewed to be in excess of that which should be reflected in Phase II costs.

50. The Commission notes Télébec's argument that large ILECs serve a greater proportion of urban centres, and that it would be inappropriate to apply the national AWFF thresholds set out in Decision 2001-238. The Commission also notes that while both companies proposed using current AWFF measures to develop their unbundled loop and residential PES access cost estimates, Télébec did not explain why its current AWFF measures were more appropriate than the national HCSA AWFF thresholds of 72 percent for copper feeder plant and 56 percent for copper distribution plant for each proposed band.

51. The Commission notes that the HCSA bands are defined uniformly across all ILECs. In the Commission’s view, the ILECs' AWFFs for these bands, including TELUS Québec and Télébec, would display similar utilization levels. In these circumstances, the Commission considers it appropriate to use the national HCSA AWFF thresholds to determine Télébec's and TELUS Québec's unbundled loop and residential PES access cost estimates in the HCSA bands, consistent with the other large ILECs.

52. With respect to the non-HCSA bands, the Commission notes that Télébec's and TELUS Québec's operating territories do not have bands with similar characteristics to Bands A and B of the other large ILECs. Accordingly, the Commission does not consider it appropriate to apply the national AWFF thresholds set out for non-HCSA bands in Decision 2001-238 of 77 percent for copper feeder plant and 60 percent for copper distribution plant, given that these AWFF levels reflect greater proportions of urban centre utilization measures compared to Télébec and TELUS Québec. In these circumstances, the Commission considers that the national HCSA AWFFs represent more suitable AWFF thresholds for Télébec's and TELUS Québec's non-HCSA bands, and finds it appropriate to use the national HCSA AWFF thresholds to determine Télébec's and TELUS Québec's unbundled loop and residential PES access cost estimates in the non-HCSA bands, consistent with Télébec's proposal.

53. The Commission notes TELUS Québec's submission that its local network consists almost entirely of distribution plant and that it would be inappropriate to apply the national AWFF averages developed based on the other large ILECs' network designs. The Commission further notes that the local network infrastructures of most ILECs, including Télébec, employ physical juncture or distribution points to connect the larger-size feeder cable to multiple smaller-size distribution cables. In the Commission's view, the overall utilization of an ILEC's local network infrastructure should not depend on whether physical distribution points have been created. In the circumstances, the Commission considers that TELUS Québec should be expected to achieve utilization levels that are similar to other large ILECs for similar operating regions.

54. The Commission notes that in its 29 October 2002 cost submission, Télébec proposed the use of the national feeder and distribution AWFFs of 72 percent and 56 percent, respectively, and feeder/distribution ratios of between 50/50 and 80/20, corresponding to effective aggregate AWFFs of between 64 percent and 69 percent. The Commission finds these AWFFs and feeder/distribution ratios to be reasonable. For TELUS Québec, the Commission considers it appropriate to use the national feeder and distribution AWFFs of 72 percent and 56 percent, respectively. However, in light of the unique nature of TELUS Québec’s local network, as outlined in paragraph 53 above, the Commission considers it appropriate to use the lower end of Télébec’s feeder/distribution ratios of 50 percent for TELUS Québec, resulting in the use of an aggregate AWFF of 64 percent for each of its bands.

55. With respect to TELUS Québec's argument that the Commission should not use the AWFF cost sensitivity results associated with different cable size mixes, the Commission notes that it has relied on TELUS Québec's proposed cable costs without altering its proposed cable size mix.

FOEs

56. While the Companies generally relied on the FOE caps set out in Decision 2001-238 to develop their unbundled loop and residential PES cost studies, the Commission notes that TELUS Québec adopted an FOE level higher than $2.50 per NAS for its residential PES cost study. The Commission notes that in its initial 28 March 2002 cost study, TELUS Québec submitted that its FOE estimate was determined based on its 2000 accounting data. The Commission further notes that in its 29 October 2002 cost update, TELUS Québec revised its FOE estimate, indicating that this update was required to capture more recent data and to reflect the 2001 inflation factor which it had previously omitted.

57. The Commission notes that based on the inflation less productivity gains realized over the 2000 to 2002 period, TELUS Québec's proposed 2000 residential PES FOE estimate would be restated to approximately $2.50 in 2002 dollars.

58. The Commission therefore considers it appropriate to maintain the Decision 2001-238 FOE caps for TELUS Québec and Télébec, established at $1.65 for unbundled loops and $2.50 for residential PES, for all bands, consistent with the other large ILECs.

Maintenance expenses

59. The Commission notes that both TELUS Québec and Télébec provided estimates of unbundled loop and residential PES maintenance expenses that were higher than the 10 percent cap of the present worth of annualized cost (PWAC) capital set out in Decision 2001-238. Télébec indicated that it used its 2000 Phase III maintenance expense data for its Utility segment expressed on a per NAS basis. By contrast, TELUS Québec's proposed maintenance expense was initially set at 10 percent of capital in its 28 March 2002 unbundled loop and residential PES cost studies, but was subsequently revised in its 29 October 2002 cost update based on TELUS Québec's 2001 accounting data associated with access facilities.

60. The Commission notes that Télébec provided little justification for its proposed maintenance expense estimates other than the claim that these expenses were those reported under its 2000 Phase III network maintenance expenses for its Utility segment and represented the expenses that were causal to loop and PES services. The Commission notes that Télébec's estimated Phase III-based maintenance expense per-NAS estimate was further adjusted to include a 20 percent benefit loading factor. Télébec's proposed Band G per-NAS maintenance expense was further multiplied by 2.75 to include a remoteness loading factor.

61. The Commission also notes that, despite being invited to do so, TELUS Québec failed to provide justification as to why the proposed maintenance expenses under its revised costing approach, which relied on the accounting-based maintenance expense data, would reflect the maintenance expense causal to loop and residential PES services.

62. In the Commission's view, the Companies' claim that the per-NAS accounting-based maintenance expenses are causal to loop and residential PES cost studies does not guarantee or justify that they represent the appropriate prospective incremental maintenance expenses that are causally-related to loop or residential PES services. For example, there are numerous other local services offered by the Companies, such as the wireless and toll interconnection services, directory and operator services, various data and private line services, high-speed Internet and other recent wideband service initiatives, which are also expected to cause maintenance expenses. The Companies did not explain how the accounting data was adjusted to exclude the maintenance activities and costs associated with those other services. The Companies also did not explain how the historical data was adjusted to reflect the appropriate current prospective incremental costs.

63. In these circumstances, the Commission considers it appropriate to maintain the Decision 2001-238 maintenance expense cap for TELUS Québec and Télébec, established at 10 percent of the capital PWACs for all bands except Band G, for the purpose of determining the loop and residential PES costs, consistent with other large ILECs. In the case of Band G, the maintenance expenses are to be capped at $20 per NAS, consistent with Decision 2001-238. Given that TELUS Québec's and Télébec's proposed maintenance expenses in Band G are at levels below the $20 per NAS threshold set in Decision 2001-238, no adjustments were made to their proposed levels in that band.

Revenue-percent charge and revenue tax calculations

64. The Commission notes that TELUS Québec proposed to apply a revenue charge rate of 4.5 percent in its Phase II cost studies, consisting of the following two elements: (a) the subsidy revenue-percent charge estimated at 1.4 percent of revenues and (b) the Quebec Telecommunications, Gas and Electricity (QTG&E) Tax representing the remaining portion of the revenue charge rate. In contrast, Télébec proposed the rate of 1.4 percent for the subsidy revenue-percent charge but included an explicit amount per NAS per band for the QTG&E Tax based on its 2000 Phase III data.

65. The Commission notes that the QTG&E Tax amount is determined by applying the current applicable tax rate of 8 percent to a company's telecommunications revenues net of deductible operating expenses. The Commission considers that TELUS Québec's above-noted method of calculating its revenue taxes underestimates the QTG&E Tax charges. Accordingly, the Commission has made the necessary adjustments to reflect the appropriate tax cost calculations for TELUS Québec. The Commission has further adjusted TELUS Québec's and Télébec's loop costs to reflect the final 2003 subsidy revenue-percent charge rate of 1.1 percent rather than the assumed 1.4 percent rate.

Proposed conduit costs

66. The conduit costs that were proposed in the Companies' loop and residential PES cost studies reflected the support structure costs associated with underground copper or fibre cabling. The Commission notes that these costs are included as part of the unbundled loop capital costs and as part of the PES access capital costs.

67. The Commission notes that TELUS Québec assumed a conduit loading factor in its cost studies, while Télébec determined explicit estimates of its conduit costs for each typical wire centre based on the replacement costs of its embedded base of conduit facilities.

68. In the Commission's view, the conduit costs estimated by TELUS Québec in its Phase II cost studies are overstated when compared to Bell Canada's and TCI's current conduit loading factors, which are currently estimated at levels below 50 percent. The Commission notes that the loading factors for the large ILECs are typically developed by determining the ratio of the incremental conduit capital expenditures to the total incremental capital expenditures of the equipment using this conduit structure.

69. Under Télébec's cost proposal, the entire embedded base of conduit facilities is costed at replacement cost, the large majority of which is then attributed to unbundled loop or local PES services. The Commission notes that such a costing methodology assumes that incremental costs are determined by applying the replacement cost to the embedded asset base. This, in the Commission's view, will overstate the incremental costs if they do not represent the most efficient growth route and/or growth technology costs. The Commission further notes that in non-growth areas, the conduit facilities may never be replaced, in which case these assets may be considered as non-fungible and the associated incremental costs of these facilities would be lower than the replacement cost.

70. In light of the above, the Commission considers it appropriate to cap the conduit costs to an amount equal to a loading factor of 75 percent for both TELUS Québec and Télébec to determine the Companies' unbundled loop and residential PES access cost estimates.

Proposed per-metre installed first costs of copper cable

71. The Commission notes that the unbundled loop facility consists primarily of outside copper cable plant and its associated support structures, such as poles and conduits. The unbundled loop plant also includes the various remote access facilities such as the Integrated Digital Loop Carrier (IDLC) systems and related fibre cable plant for local loops that are served off remotes. In this proceeding, the Commission observed large discrepancies in the proposed per-metre copper cable installed first costs (IFCs) between TELUS Québec's initial and subsequent cost submissions, and further between TELUS Québec's subsequent costs and those previously submitted by TCI for Alberta and British Columbia for the year 2000.

72. The Commission notes that significant increases were proposed by TELUS Québec for most of the per-metre copper cable IFCs between its initial 28 March 2002 cost study and its subsequent 29 October 2002 cost update. For example, TELUS Québec's proposed average per-metre IFCs were increased by approximately 20 percent for aerial copper cable, and by approximately 70 percent for buried copper cable. TELUS Québec indicated that its per-metre copper cable IFCs had been updated to correct certain anomalies detected at the disaggregated component level and to also reflect 2002 unit costs compared to its earlier cost submissions which reflected 2001 unit costs. The Commission notes that TELUS Québec did not provide an explanation for the anomalies or the related cost adjustments.

73. The Commission notes that the IFC increases were primarily attributable to increases in the average installation and engineering labour hours and costs, offset slightly by reductions in the material costs. For example, TELUS Québec's 25-pair, 26-gauge aerial cable IFC increased by 17 percent in its 29 October 2002 cost update, compared to its initial 28 March 2002 cost study, led by an increase in the labour-related costs of 32 percent and offset slightly by a material cost reduction. Similarly, increases of 88 percent were observed for TELUS Québec's 25-pair, 26-gauge buried cable IFC in its 29 October 2002 cost update, primarily as a result of an increase in the associated labour-related costs of 175 percent. TELUS Québec provided no explanations to justify its increases in the labour-related costs, which in the Commission's view, should be relatively stable with the exception of the annual wage increases. The Commission further notes that similar IFC increases were proposed for most of TELUS Québec’s copper cable sizes and types.

74. In light of the above, the Commission considers it appropriate to use the historical 2001 unit costs[3] used by TELUS Québec in its 28 March 2002 cost study as a proxy for its 2002 unit costs to determine TELUS Québec's unbundled loop and residential PES access cost estimates.

75. The Commission further notes the high per-metre copper cable IFCs proposed by Télébec compared to both vintages of TELUS Québec's proposed IFCs. Moreover, Télébec's proposed average per-metre copper cable IFCs were generally reported to be 50 percent higher or more compared to those proposed by TELUS Québec in its 28 March 2002 cost study.

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[3] TELUS Québec's historical 2001 unit costs were provided by the company in its 13 June 2002 submission.

76. The Commission also notes several discrepancies in the assumed material costs and installation and engineering costs between TELUS Québec and Télébec. For example, Télébec's assumed material costs were nearly double TELUS Québec's proposed current material costs for its 25-pair cable. Similarly, Télébec's assumed per-metre labour-related costs for its 25-pair cable were approximately 50 percent higher than those assumed by TELUS Québec in its 28 March 2002 cost study.

77. The Commission finds that no evidence has been presented on the record of this proceeding to indicate that Télébec's per-metre copper cable prices, associated installation and engineering costs would be significantly different from TELUS Québec's.

78. In the circumstances, the Commission considers it appropriate to use TELUS Québec's historical 2001 unit costs as a proxy for Télébec's 2002 per-metre copper cable unit costs to determine Télébec's unbundled loop and residential PES access cost estimates.

Télébec's proposed remote access infrastructure costs

79. The Commission notes that Télébec's proposed costs for common structure equipment at the remote access sites such as outside plant remote cabinets or huts, pole cabinets and associated power reflected the replacement costs of each common structure, of which 100 percent was assigned to the company's local PES service. Similarly, Télébec's proposed NAS-related remote access costs such as remote line concentrator modules and line cards reflected the replacement costs of each resource component, of which 78 percent was assigned to the company's local PES service, with the remaining 22 percent assigned to the company's toll services. The Commission further notes that Télébec's response to a Commission interrogatory revealed that the above remote access equipment costs were generally based on 2000 unit cost data. In the Commission's view, such a costing approach overestimates the Phase II causal incremental costs as set out below.

80. First, Télébec's costing approach assumes that the incremental costs are established by applying the replacement cost to the embedded base of facilities at the various remote access sites which, in the Commission's view, may not represent the appropriate incremental cost reflective of the most efficient growth route and/or growth technology solution.

81. Second, under its proposal, Télébec has assigned the entire costs of the estimated NAS-related remote access components to the company's local PES and toll services and the entire costs of the remote access common structure equipment to the company's local PES services. The Commission notes that numerous other local services offered by Télébec will make use of the NAS-related remote access components. These include local optional services, wireless call-origination and call-termination services, directory assistance and other operator services, data services, and dial-up Internet. With respect to the proposed common structure equipment, the Commission expects that the above-noted services along with the company's toll services, high-speed Internet and other emerging wideband or data services will also make use of this equipment at the remote access sites. In light of this, the Commission considers it appropriate to apply adjustments to Télébec's proposed remote access costs to reflect the shared use of such equipment and/or facilities by other company services, similar to the capacity costing approach.

82. With respect to Télébec's assumption to use 2000 unit cost data as a proxy for 2002 data, the Commission notes that recent data furnished by a number of the other large ILECs in the proceeding initiated by *Regulatory framework for second price cap period*, Telecom Decision CRTC 2002-34, 30 May 2002 regarding updated cost studies for the Access Tandem (AT) service, indicates that transport costs have dropped by over 40 percent during the period 1996 to 2002. Similarly, recent costing data furnished by a number of the other large ILECs in a follow-up proceeding to *Direct Connection service*, Telecom Decision CRTC 2003-83, 17 December 2003 regarding the Direct Connection (DC) service indicates that switching costs have dropped by between 5 percent and 20 percent during the period 2000 to 2003. The Commission, therefore, considers that it is not reasonable nor appropriate to use 2000 unit costs as a proxy for 2002 transport costs.

83. In light of this, the Commission considers it appropriate to apply adjustments to Télébec's proposed remote access costs to reflect 2002 unit costs. Accordingly, the Commission considers it appropriate to apply a -35 percent adjustment to Télébec's proposed remote access common structure costs and a -20 percent adjustment to Télébec's proposed NAS-related remote access costs to provide a more appropriate representation of the causally-related current incremental Phase II capital costs associated with remote access equipment and/or facilities.

Télébec's proposed residential PES switching and transport costs

84. With respect to Télébec's residential PES Phase II cost studies, the Commission notes that the proposed costs of the company's digital multiplex system (DMS) switching components and various transport components such as the traffic-driven costs associated with synchronous optical network (SONET) transport systems and associated fibre costs generally reflected the replacement costs of each switching and transport resource component, of which 78 percent was assigned to the company's local PES, with the remaining 22 percent being assigned to the company's toll services. The Commission further notes that Télébec's response to a Commission interrogatory revealed that the switching and transport equipment costs were generally based on 2000 unit cost data. In the case of DMS software, Télébec indicated that the costs were based on its accounting data.

85. The Commission notes that Télébec's proposed costs for its switching and transport components are assigned entirely to the company's local PES and toll services. The Commission considers that other company services such as dial-up Internet service, the wireless call-origination/termination services, local optional services, directory assistance and other operator services, and certain data services will make use of these switching and transport resources. Furthermore, the high-speed Internet and other emerging wideband or data services will also make use of the transport components. Similar to the approach used to determine the remote access costs, the Commission considers it appropriate to apply adjustments to Télébec's proposed PES switching and transport costs to reflect the shared use of such equipment and/or facilities by other company services, similar to the capacity costing approach.

86. With respect to Télébec's assumption to use 2000 unit cost data as a proxy for 2002 data, the Commission notes the above discussion regarding recent price reductions observed for similar equipment in the DC and AT service proceedings. The Commission also notes Télébec's assumption to estimate its DMS software cost based on accounting data, which is expected to overestimate the current replacement costs. In light of this, the Commission considers it appropriate to apply adjustments to Télébec's proposed switching and transport costs to reflect 2002 unit costs.

87. Accordingly, the Commission considers it appropriate to apply a -20 percent adjustment to Télébec's proposed switching costs and a -35 percent adjustment to Télébec's proposed transport costs to reflect the appropriate causally-related current incremental Phase II capital costs associated with these switching and transport equipment and/or facilities.

TELUS Québec's proposed residential PES switching and transport costs

88. The Commission notes that TELUS Québec indicated that its residential PES switching and transport costs were based on TCI's model and unit costs. The Commission further notes that TELUS Québec's response to a Commission interrogatory revealed that many of the switching and transmission installed first costs used were based on 1995 or 1996 vintage data. The Commission compared this unit cost information with Bell Canada's 2000 unit cost data for a subset of the equipment (i.e., remote access equipment), and found that the 2000 data was on average 20 percent to 35 percent lower than the 1996 unit cost data. For other types of equipment, there was no indication of the vintage of the data and no comparison could be made.

89. In light of this, the Commission considers it appropriate to apply a -20 percent adjustment to TELUS Québec's proposed switching and transport capital costs to reflect 2002 unit costs.

Total residential PES costs

90. The Commission notes that both TELUS Québec and Télébec provided their residential PES cost estimates as at 1 January 2002, based on a five-year study for the period 1 January 2002 to 31 December 2006. The Commission further notes that the proposed residential PES cost studies excluded inflation and productivity factors and the contribution revenue-percent charge, consistent with Decision 2001-238 costing specifications.

91. The Commission notes that TELUS Québec's and Télébec's residential PES costs determined in this Decision, as set out in Attachment 1, are based on TELUS Québec's 13 June 2002 submission and Télébec's 29 October 2002 submission, as adjusted to reflect the costing determinations in this Decision. The Commission finds that the residential PES costs determined in this Decision for the purpose of calculating TELUS Québec's and Télébec's subsidy requirements are necessary and appropriate to ensure that the national subsidy fund established pursuant to Decision 2000-745 will operate in a manner consistent with the objectives of the *Telecommunications Act* (the Act).

Rates for local interconnection and unbundled network components

92. In this proceeding, the Companies were expected to file proposed tariff pages, with supporting cost studies, in order to establish company-specific rates for local interconnection and unbundled network components.

Proposed tariffs were expected to be filed for the following services:

- monthly rates for unbundled local loops;
- service charges for unbundled local loops, fixed rate (per order);

- service charges for unbundled local loops, variable rate (per loop);
- service charge for loop selection;
- service charge for loop modification;
- monthly rates for loop connecting links (per 100 links);
- service charge for loop connecting links (per 100 links);
- monthly rates for common channel signalling 7 (CCS7);
- service charge for CCS7;
- monthly rates for connecting link riser space;
- monthly rates for relay service;
- service charge for relay service;
- monthly rates for 9-1-1 service (per NAS/working telephone number (WTN));
- monthly rates for 9-1-1 service (per trunk);
- service charge for 9-1-1 service;
- monthly rates and service charges for traffic imbalance service;
- monthly rates and service charges for EAS termination service;
- monthly rates and service charges for toll transit service provided to CLECs and/or inter-exchange carriers (IXCs) (for delivery of toll traffic to each other via the company's network);
- monthly rates and service charges for CCS7 transit service provided to CLECs, WSPs and IXCs to deliver CCS7 signalling messages between two different carriers; and
- monthly rates and service charges for access lines to CPTSP, and a standard service agreement.

Positions of parties

93. Mr. Ménard submitted that Télébec should be required to provide interconnection at the wire centre where loops are served by remote access systems, requiring that Télébec upgrade its existing infrastructure.

94. Télébec submitted that it would not be able to provide costing in support of its proposed rates, other than the costing submitted in support of its unbundled loop rates. Télébec indicated that some of its proposed rates were based on rates previously approved for Bell Canada.

95. Télébec submitted that the total capital costs of IDLC overlay systems to permit loop extraction at the wire centre would be prohibitive. Télébec indicated, however, that in order to allow the unbundling of local loops in those areas served by remote access equipment, it would be willing to allow CLECs the ability to install copper junction cables between access networks, which would be situated near the company's access equipment and the distribution network.

96. TELUS Québec submitted that it had not provided costing in support of its proposed rates, other than those submitted in support of its unbundled loop rates. TELUS Québec indicated that some of its proposed rates were based on the average service rates previously approved for other ILECs in the Maritimes.

97. TELUS Québec submitted that it did not include costs of IDLC overlay systems nor did it furnish cost studies to provide an estimate of the per-loop cost of such overlay systems. TELUS Québec further indicated that, should a competitor request an IDLC overlay system service, it would file proposed tariff pages with costing support.

Commission's analysis and determinations

Monthly rates for unbundled local loops

98. The Commission notes that both TELUS Québec and Télébec provided their unbundled loop cost studies based on the assumption that local loops served by remote access or IDLC equipment would not be unbundled at the wire centre in light of the prohibitive costs of the IDLC overlay systems to permit loop extraction at the wire centre. The Commission further notes Télébec's position that it would be willing to allow CLECs to install copper junction cables between access networks, situated near the company's distribution point.

99. The Commission notes that this proposed interconnection arrangement is comparable to that adopted for the NBTel Inc. (NBTel) region in Decision 98-22. In that Decision, the Commission exempted the NBTel region from the requirement to provide unbundled loops at the wire centre for loops served off IDLCs due to the excessive cost impacts of the IDLC solution in that territory. The Commission, however, notes that NBTel's unbundled loop capital costs were accordingly reduced by 10 percent, to reflect the fact that loop plant without the IDLC systems would be made up of shorter and less costly loop configurations.

100. The Commission expects that the costs associated with the required IDLC overlay systems in the Companies' territories to permit loop extraction at the wire centre for loops served off IDLCs will be significant. The Commission therefore considers it appropriate to adopt TELUS Québec's and Télébec's loop cost proposals of excluding the IDLC overlay systems and associated costs from the unbundled loop cost studies. However, the Commission advises the Companies that they should be prepared to allow CLECs to install copper junction cables between access networks situated near each of the company's distribution points, on request. The Commission notes that once a request is made, the Companies should be prepared to file tariffs within 30 days of such request.

101. The Commission further considers it appropriate to reduce TELUS Québec's and Télébec's unbundled loop capital costs by 10 percent to reflect that the loop plant without the IDLC systems will be made up of shorter and less costly loop configurations, similar to the unbundled loop capital cost adjustments rendered for the NBTel region in Decision 98-22.

102. The Commission notes that the loop rates will be approved effective the date of this Decision. The Commission has accordingly restated the 2002 loop cost estimates to current 2005 cost estimates, by applying the Companies' inflation minus productivity factors over the period 2002 to 2005.

103. The Commission notes that the Companies' proposed Type A unbundled local loop rates were based on their proposed local loop costs plus a 25 percent mark-up, consistent with Decision 2002-43. The Commission therefore **approves,** for TELUS Québec and Télébec, the Type A unbundled loop rates, based on the Type A unbundled loop cost determined in this Decision plus a 25 percent mark-up, effective the date of this Decision. The Commission notes that the revised Type A unbundled loop costs determined in this Decision are based on TELUS Québec's 13 June 2002 submission and Télébec's 29 October 2002 submission, as adjusted to reflect the costing determinations in this Decision, including the above-noted -10 percent adjustment to the capital costs.

104. The Commission finds that the Type A unbundled loop rates, based on the unbundled loop costs determined in this Decision plus a 25 percent mark-up, are just and reasonable and are consistent with the objectives of the Act.

105. In light of the above, the Commission **approves, on a final basis**, effective the date of this Decision, the Type A unbundled loop rates for TELUS Québec and Télébec set out in Attachment 2 to this Decision. The Commission also directs TELUS Québec and Télébec to issue tariff pages for the unbundled loop rates, within 30 days of the date of this Decision.

Rates for other local interconnection services

106. The Commission notes that the Companies proposed rates for most of the other local interconnection services as directed in Public Notice 2001-69. However, the Commission notes that TELUS Québec did not propose competitor service rates for services such as CCS7 interconnection, Message Relay or 9-1-1, and Télébec did not propose competitor service rates for services such as loop selection and loop modification. The Commission further notes that neither of the companies provided cost studies to support any of their other local interconnection service rates.

107. The Commission notes that TELUS Québec indicated that CCS7 services would be provided on its behalf by another service provider. The Commission considers that, in the event that a service is not provided directly by the Companies, proposed tariffs should still include the service by making reference to an other ILEC tariff or by identifying the specific pass-through charge. As such, the Commission considers that TELUS Québec must file competitor tariffs for CCS7 interconnection, Message Relay and 9-1-1 services. The Commission also considers that Télébec must file tariffs for loop selection and loop modification service charges.

108. In view of the absence of costing support filed by the Companies, and in order to accelerate the introduction of local competition within the Companies' territory, the Commission considers that it would be appropriate to benchmark their rates to those approved for Bell Canada, which operates in the same province. The Commission notes, however, that Bell Canada's Category I Competitor service rates are based on Phase II costs plus a 15 percent mark-up, while those for the Companies are to be based on Phase II costs plus a 25 percent mark-up. As such, the Commission considers it appropriate to allow the Companies to adjust Bell Canada's current local interconnection and unbundled network component service rates (other than local loop rates which were addressed earlier in this Decision) to include an additional multiplicative factor of 8.7 percent in order to convert Bell Canada's rates based on Phase II costs plus a 15 percent mark-up to Phase II costs plus a 25 percent mark-up.

109. In light of the above, the Commission directs Télébec and TELUS Québec to file for approval, within 30 days of the date of this Decision, proposed tariff pages for other local interconnection services, including those identified in paragraph 106, using the terms and conditions already approved for Bell Canada, but with the associated rates marked up by 8.7 percent, or in the alternative, rates that are based on company-specific costs plus a 25 percent mark-up, with supporting cost justification.

Monthly rates and service charges for access lines to CPTSP

110. In *Local payphone competition in the territory of TELUS Communications (Québec) Inc. - Request by Bell Canada*, Telecom Order CRTC 2003-390, 25 September 2003, the Commission approved on an interim basis the local pay telephone access line rates proposed by TELUS Québec in Public Notice 2001-69, following a request by Bell Canada.

111. The Commission notes that Télébec proposed rates for access lines to CPTSP with a standard service agreement but did not provide costing support. TELUS Québec also proposed rates for access lines to CPTSP, without costing support, as well as a standard service agreement based on the tariff and agreement for the same service approved for Bell Canada.

112. The Commission considers that, consistent with its determinations for other local interconnection services, the rates for this service should be established based on Bell Canada's rates plus an 8.7 percent mark-up.

113. In light of the foregoing, the Commission directs Télébec and TELUS Québec to file for approval, within 30 days of the date of this Decision, proposed tariff pages for access lines to CPTSP using the terms and conditions already approved for Bell Canada with the associated rates marked up by 8.7 percent, or in the alternative, rates that are based on company-specific costs plus a 25 percent mark-up, with supporting cost justification.

Quality of service

Background

114. In *Quality of service indicators for use in telephone company regulation*, Telecom Decision CRTC 97-16, 24 July 1997, the Commission established Q of S indicator standards. The Commission also considered that TELUS Québec and Télébec would be regarded as rural for reporting purposes.

115. In *Long-distance competition and improved service for Northwestel customers*, Decision CRTC 2000-746, 30 November 2000 (Decision 2000-746), the Commission identified remote communities within Northwestel Inc.'s (Northwestel's) serving territory and established specific Q of S standards for that company. Then, in *CRTC creates new quality of service indicators for telephone companies*, Decision CRTC 2001-217, 9 April 2001, the Commission determined that Northwestel should report some of its Q of S indicators at the community level.

116. In Decision 2001-238, the Commission directed the large ILECs to report Q of S indicators such that HCSA bands were considered as rural and non-HCSA bands were considered as urban. In Decision 2002-43, the Commission stated that the same Q of S indicators applicable to the large ILECs should also apply to TELUS Québec and Télébec.

Positions of parties

117. Télébec argued that the low population densities and the long distances between exchanges within its territory increased its operational costs and also limited the possibility of any cost reductions. As such, Télébec proposed that its entire serving territory be considered rural, other than those communities deemed remote, in order to apply Q of S indicators. For remote communities, Télébec argued that its remote band had the same characteristics as Northwestel's remote communities and proposed that the remote community Q of S standards established for Northwestel in Decision 2000-746 be applied to its Band G exchanges. TELUS Québec indicated that it could not justify different Q of S standards.

118. In its reply comments, Télébec amended its position by proposing to lower the rural service objectives for Q of S Indicator 2.1: Out-of-Service Trouble Reports Cleared Within 24 Hours (Q of S Indicator 2.1) from 80 percent or more cleared within 24 hours to 75 percent or more cleared within 24 hours, rather than applying the standards applicable to remote communities for that indicator. Télébec maintained that the remaining remote community Q of S standards should be applied to its Band G exchanges.

119. TELUS Québec revised its position and supported Télébec's proposal to apply all the remote community Q of S standards to its Band G exchanges. TELUS Québec indicated that it would be inappropriate to require the same repair objectives in its Band G as those for rural regions that were accessible by road.

Commission's analysis and determinations

120. With respect to Télébec's proposal to consider all of its territory as rural, the Commission notes that the company originally proposed that all of its exchanges be deemed as HCSAs, which would have resulted in rural Q of S reporting requirements for its territory, other than remote communities. However, the Commission notes that, pursuant to its determinations on rate band structure, Télébec has non-HCSA bands within its territory. As such, the Commission finds that, consistent with the other large ILECs, Télébec should apply urban Q of S indicators to its non-HCSA bands.

121. With respect to the Companies' proposal to apply the remote community Q of S standards to their Band G exchanges, the Commission notes that although Northwestel has specific Q of S standards for its remote communities, Northwestel also has specific Q of S reporting standards at the community level. The Commission notes that neither party addressed the possibility of community level reporting.

122. The Commission considers that in order to apply remote community Q of S standards, the associated reporting requirements are also necessary. Consequently, the Commission finds that it would not be appropriate to apply the remote community Q of S standards to the Companies' Band G exchanges at this time. The Commission considers, however, that the Companies may file, at a later date, an application to have remote community Q of S standards apply to their Band G exchanges if the associated community level reporting is also proposed.

123. With respect to Télébec's proposal to lower the standard for Q of S Indicator 2.1, the Commission considers that there is insufficient evidence to demonstrate that Télébec has made every reasonable effort to attain the 80 percent or more cleared within 24 hours standard in order to justify the standard being lowered. Consequently, the Commission finds that it would not be appropriate to lower Télébec's Q of S Indicator 2.1 to 75 percent or more cleared within 24 hours.

Business primary exchange service subsidy

124. In Decision 2001-238, the Commission concluded that subsidies should not be extended to business PES in HCSAs.

Positions of parties

125. Télébec indicated that it did not consider it appropriate to extend the subsidy mechanism to business PES service. TELUS Québec also expressed the view that subsidies should not be extended to business PES in HCSAs. However, TELUS Québec requested that if a business PES rate did not recover cost, the Commission should allow it to raise business PES rates so that they are compensatory.

Commission's analysis and determination

126. The Commission notes that pursuant to Decision 2002-43, business PES was given a price cap basket constraint set at inflation with no productivity offset. These services were also subject to a rate element constraint limiting individual rate increases to 10 percent per year. Consequently, the Commission considers that the Companies have the ability to raise business PES rates in HCSAs in order to ensure that they are compensatory.

127. In light of the above, the Commission finds that it is not appropriate to extend subsidies to business PES in HCSAs within the Companies' territories.

Other matters

Positions of parties

128. Both Mr. Ménard and RTS raised concerns regarding the implementation of competition in Télébec's territory and requested that Télébec be required to upgrade its network in order to ensure that competitors had access to all services.

129. While Mr. Ménard raised specific issues regarding the provisioning of high-speed Internet access services, RTS raised issues regarding the telecommunications needs of the Cree communities and filed, in confidence, an independent study to support its position.

130. Télébec requested that RTS' study be provided on the public record.

Commission's analysis and determinations

131. The Commission considers that its determinations resulting from this proceeding address those matters within the scope of Public Notice 2001-69. The Commission finds that it is not appropriate to address those matters raised by Mr. Ménard and RTS that are beyond the scope of this proceeding.

132. The Commission notes that requests for disclosure of information for which confidentiality has been claimed are assessed in light of sections 38 and 39 of the Act and section 19 of the *CRTC Telecommunications Rules of Procedure*. In the case of each request, the public interest in disclosure is weighed against the specific direct harm, if any, likely to result from disclosure. In light of its finding that certain matters raised by RTS are outside the scope of the proceeding, including all of those related to the RTS study, the Commission does not consider there to be any public interest warranting the disclosure of RTS' study for the purposes of this proceeding. Accordingly, the Commission **denies** Télébec's request to make publicly available the RTS study.

Implementation issues

A. Subsidy requirements and the National Contribution Fund

Introduction

133. In *Final 2002 revenue-percent charge and related matters*, Telecom Decision CRTC 2002-71, 22 November 2002, the Commission approved final 2002 subsidy requirements for TELUS Québec and Télébec.

134. With the establishment of the HCSA rate band structure and the corresponding Phase II residential PES costs, the following subsidy issues can now be addressed:

- Transition subsidy;
- Service improvement plan (SIP) funding;
- The 2003/2004 subsidy requirements and related funding adjustments; and
- The subsidy process for 2005 and beyond.

Transition subsidy

135. In Decision 2002-43, the Commission determined that, until a banding structure and associated band costs had been approved for TELUS Québec and Télébec, the Companies should use the national average Phase II costs and the corresponding band structure for subsidy purposes. The Commission also determined the going-in revenue requirements for TELUS Québec and Télébec to be $13.6 million and $15.7 million, respectively.

136. The Commission notes that Télébec was provided an interim transition subsidy from the National Contribution Fund (NCF) to make up for the difference between Télébec's going-in revenue requirement and the subsidy amount calculated using the national average Phase II costs and the corresponding band structure. TELUS Québec was not provided with an interim transition subsidy because the subsidy amount calculated based upon the national average Phase II costs and the corresponding band structure was greater than its going-in revenue requirement.

137. In Decision 2002-43, the Commission determined that the Companies should apply an annual inflation increase less productivity offset (collectively known as an (I-X) adjustment) to the annual costs in their subsidy calculations and to the revenues associated with their baskets of capped services. The effective date of the (I-X) adjustment is 1 August of each year, so that the annual subsidy calculations are for the period 1 August of one year to 31 July of the following year. The Commission notes that, in the case of Télébec, its (I-X) adjustment was to be applied to its transition subsidy until its transition subsidy reached zero, instead of to the annual costs in its subsidy calculations and to the revenues associated with its baskets of capped services.

138. With the establishment of the HCSA rate band structure and the corresponding Phase II residential PES costs, the issue of whether or not TELUS Québec and/or Télébec should receive transition subsidy needs to be reviewed.

139. With respect to TELUS Québec, the Commission notes that the Phase II residential PES costs in Attachment 1 are greater than the national average Phase II costs. Therefore, TELUS Québec is not entitled to transition subsidy because the subsidy amount calculated based upon its Phase II residential PES costs in Attachment 1 and HCSA rate band structure would be greater than its going-in revenue requirement.

140. With respect to Télébec, the Commission notes that Télébec's 2002 subsidy amount recalculated using its Phase II residential PES costs in Attachment 1 and HCSA rate band structure would be $14.880 million. Since $14.880 million is less than Télébec's going-in revenue requirement of $15.7 million, Télébec is entitled to $0.820 million of transition subsidy.

141. While Decision 2002-43 directed Télébec to apply its annual (I-X) adjustment to its transition subsidy until the transition subsidy reached zero, with the normal (I-X) adjustments being suspended, the Commission notes that the application of this process is administratively difficult because the 2002 (I-X) adjustment would only be partially applied to the transition subsidy with the remaining portion being applied to the annual costs in the subsidy calculations and to the revenues associated with Télébec's baskets of capped services.

142. The Commission is of the opinion that, rather than applying Télébec's 2002 (I-X) adjustment to its transition subsidy, the annual costs in the subsidy calculations and to the revenues associated with its baskets of capped services, it would be simpler to account for the transition subsidy through the deferral account, similar to the treatment of an exogenous factor in the pricing regime established by Decision 2002-43.

143. Therefore, the Commission considers that Télébec should apply the normal (I-X) adjustment to the annual costs in its subsidy calculations and to the revenues associated with its baskets of capped services, effective 1 August 2002, with the transition subsidy being handled through the deferral account. The Commission notes that details on the deferral account process can be found below.

144. Based upon the above, the Commission has applied Télébec's 2002 (I-X) adjustment to the annual costs in its subsidy calculations. The Commission notes that Télébec's 2003 and 2004 annual (I-X) adjustments were also applied against Télébec's annual costs in its subsidy calculations, consistent with Decision 2002-43, and that Télébec should apply future (I-X) adjustments to the annual costs in future subsidy calculations.

Service improvement plan funding

145. In *Société en commandite Télébec – Follow-up to Decision 2002-43 – Service improvement plan*, Telecom Decision CRTC 2004-77, 18 November 2004 (Decision 2004-77), the Commission approved initial interim annual SIP funding for Télébec of $0.627 million, effective 1 January 2003, based upon the band structure associated with the national average Phase II costs.

146. In *TELUS Communications Inc. – Follow-up to Decision 2002-43 – Service improvement plan*, Telecom Decision CRTC 2004-78, 18 November 2004 (Decision 2004-78), the Commission approved interim annual SIP funding for TELUS Québec of $0.087 million, effective 1 January 2004, based upon the band structure associated with the national average Phase II costs.

147. The Commission notes that the SIP funding was only approved on an interim basis pending a determination in this proceeding.

148. Since the Commission is establishing an HCSA rate band structure for TELUS Québec and Télébec that matches the band structure associated with the national average Phase II costs, the initial interim SIP funding for Télébec and the interim SIP funding for TELUS Québec can be finalized.

149. In Decision 2002-43, the Commission directed the Companies to add their HCSA Phase II SIP costs to the costs that flow into their subsidy calculations. The Commission notes that although the HCSA Phase II SIP costs are added to the subsidy calculations in the first year of the SIP, in subsequent years the HCSA Phase II SIP costs are already included in the annual costs that flow into the subsidy calculations from the previous year.

150. The Commission notes that the HCSA Phase II SIP costs to be included in the subsidy per residential NAS calculations by TELUS Québec and Télébec, which correspond to the interim SIP funding approved by the Commission in Decisions 2004-77 and 2004-78, are:

	TELUS Québec	**Télébec**
Band E	$0.06	$0.80
Band F	$0.04	$0.33
Band G	n/a	$0.40

151. The Commission notes that Télébec's SIP funding should be added to the annual costs in its 2003 subsidy calculations because its SIP funding was effective 1 January 2003, and that TELUS Québec's SIP funding should be added to the annual costs in its 2004 subsidy calculations because its SIP funding was effective 1 January 2004.

152. The Commission **approves, on a final basis**, the HCSA Phase II SIP costs for Télébec and TELUS Québec, as outlined in the above table, effective 1 January 2003 and 1 January 2004, respectively.

2003 and 2004 subsidy requirements and related funding issues

153. In Decision 2002-43, the Commission outlined the annual subsidy calculations to be performed by TELUS Québec and Télébec to determine the amount of subsidy per residential NAS to be received from the NCF. The subsidy calculations included an (I-X) adjustment, a 15 percent mark-up on costs, the cost recovery of the revenue-percent charge and reductions for average local service rates, and an implicit subsidy amount of $5 per month associated with local optional features.

154. In *Final 2003 revenue-percent charge and related matters*, Telecom Decision CRTC 2003-84, 19 December 2003, the Commission approved interim 2003 subsidy requirements for TELUS Québec and Télébec, and in *Final 2004 revenue-percent charge and related matters*, Telecom Decision CRTC 2004-81, 9 December 2004, the Commission approved interim 2004 subsidy requirements for TELUS Québec and Télébec.

155. The Commission notes that the interim 2003 and 2004 subsidy requirements, including SIP funding and, in the case of Télébec, transition subsidy, were:

	TELUS Québec	**Télébec**
	($ million)	
Interim 2003	$11.822	$10.947
Interim 2004	$11.135	$ 7.950

156. When the established HCSA rate band structure, the corresponding Phase II residential PES costs and SIP funding are included in the 2003 and 2004 subsidy calculations, in accordance with Decision 2002-43, the final 2003 and 2004 subsidy requirements are:

	TELUS Québec	**Télébec**
	($ million)	
Final 2003	$15.019	$13.919
Final 2004	$14.341	$13.275

157. The Commission notes that, as outlined in the transition subsidy section above, Télébec's transition subsidy will be handled as part of the deferral account process and, therefore, no transition subsidy is included in the above subsidy requirements.

158. The Commission **approves** final 2003 subsidy requirements of $15.019 million for TELUS Québec and $13.919 million for Télébec, and final 2004 subsidy requirements of $14.341 million for TELUS Québec and $13.275 million for Télébec.

159. The Commission notes that, when the final 2003 and 2004 subsidy requirements are compared to the interim 2003 and 2004 subsidy requirements, TELUS Québec is entitled to an additional $6.403 million and Télébec is entitled to an additional $8.297 million.

160. The Commission directs the Central Fund Administrator (CFA) to remit additional 2003 and 2004 subsidy in the amount of $6.403 million to TELUS Québec and $8.297 million to Télébec within 10 days from the date of this Decision.

Subsidy process for 2005 and beyond

161. With the establishment of the HCSA rate band structure and corresponding Phase II residential PES costs, TELUS Québec and Télébec will receive their subsidy on a going-forward basis (i.e., effective 1 January 2005) on a subsidy per residential NAS basis, consistent with the other large ILECs.

162. In order for TELUS Québec and Télébec to receive their subsidy based upon subsidy per residential NAS information, TELUS Québec and Télébec must report monthly residential NAS information for Bands E, F, and G to the CFA. The CFA will then make the necessary calculations and payments to TELUS Québec and Télébec, based upon the subsidy per residential NAS and the monthly residential NAS reported.

163. The Commission directs:

- TELUS Québec and Télébec to report residential NAS for Bands E, F, and G to the CFA, on a monthly basis, effective 1 January 2005 (i.e., for the January 2005 reporting period); and

- The CFA to remit monthly subsidy to TELUS Québec and Télébec based upon the subsidy per residential NAS times the monthly residential NAS reported in the corresponding HCSA bands, effective 1 January 2005 (i.e., for the January 2005 reporting period).

164. Based upon the subsidy calculations used to determine the final 2004 subsidy requirements, TELUS Québec's and Télébec's monthly subsidy per residential NAS are:

	TELUS Québec	**Télébec**
Band E	$15.58	$18.25
Band F	$ 3.88	$ 6.54
Band G	$49.08	$16.64

165. The Commission **approves, on an interim basis,** the subsidy per residential NAS amounts for TELUS Québec and Télébec, outlined in the above table, effective 1 January 2005.

166. In order to assist TELUS Québec and Télébec with their 2005 subsidy calculations, the Commission notes that the 1 January 2005 residential PES costs per month (i.e., the costs after the 1 August 2004 (I-X) adjustment) are:

	TELUS Québec	**Télébec**
Band E	$38.11	$47.14
Band F	$27.94	$36.58
Band G	$67.24	$43.55

B. Télébec's price cap commitments

167. As noted earlier, the Commission established the price regulation framework applicable to the Companies in Decision 2002-43. This price regulation framework established baskets of telecommunications services with associated price cap commitments. The service revenues assigned to the Residential Local Services in non-HCSAs basket and the Other Capped Services basket were made subject to an (I-X) constraint, while competitor services were subject to an (I-X) constraint at the rate element level.

168. In Decision 2002-43, the Commission also introduced a mechanism requiring the Companies to establish a deferral account. The Companies were directed to assign to that account, in each year of the price cap period, an amount equal to any revenue reduction that would otherwise be required under the (I-X) constraint for the Residential Local Services in non-HCSAs basket.

169. In Decision 2002-43, the Commission further determined that Télébec's residual going-in revenue requirement shortfall would be funded from a transitional subsidy from the NCF. The Commission determined that it would suspend the application of all (I-X) constraints until the revenue requirement shortfall was fully depleted. However, once the shortfall was depleted, Télébec would be required to contribute to its deferral account the amounts associated with the (I-X) constraint on the Residential Local Services in non-HCSAs basket. Similarly, the Commission determined that the application of all other (I-X) constraints would be reinstituted once the shortfall was depleted.

170. In Decision 2004-77, the Commission approved, on an interim basis, an exogenous factor adjustment of $483,500 applicable to the Residential Local Services in non-HCSAs basket, for the recovery of non-HCSA SIP costs, pending the issuance of a decision in this proceeding.

Commission's analysis and determinations

171. The Commission notes that Télébec's residual going-in revenue requirement shortfall, resulting from the subsidy amounts established in this proceeding, is significantly smaller than previously anticipated. As a result, the Commission considers it appropriate to revise the transitional subsidy mechanism established for Télébec in Decision 2002-43.

172. The Commission considers that Télébec's (I-X) constraints to the various baskets and rate elements should be reinstated effective 1 August 2002. The Commission considers, however, that the associated revenue reductions that would have been required during that period need to be addressed.

173. The Commission finds that, in light of Télébec's revenue requirement shortfall and SIP costs in non-HCSAs, it would be appropriate to transfer the (I-X) constraint revenue reductions during the period of 1 August 2002 to 31 July 2005, the end of the current price cap year, to the company's deferral account. The Commission finds that these deferral account balances are to be used to compensate Télébec's smaller than previously anticipated revenue requirement shortfall and SIP costs in non-HCSAs.

174. In light of the above, the Commission directs Télébec, within 45 days of the date of this Decision, to:

- file updates to the service band limit (SBL) and service band index (SBI) for the 2002, 2003, and 2004 price cap years, with supporting calculations, formulae and spreadsheets, for each basket/sub-basket of capped services;
- place the cumulative revenues that were expected as a result of the (I-X) constraints in the 2002, 2003, and 2004 price cap years into its deferral account; and
- deduct with supporting calculations, formulae and spreadsheets the effects of the revenue requirement shortfall and SIP costs in non-HCSAs from the deferral account balances.

Secretary General

Attachment 1

Residential PES costs per month ($ 2002)

	Band C	**Band D**	**Band E**	**Band F**	**Band G**
TELUS Québec	19.40	26.05	39.90	29.26	70.51
Télébec	28.66	27.32	48.62	38.03	45.26

Attachment 2

Unbundled loop rates per month ($ 2005)
(Based on Phase II costs + 25%)

Type A loops	Band C	Band D	Band E	Band F	Band G
TELUS Québec	15.28	21.48	33.39	23.78	25.78
Télébec	23.63	20.24	48.21	31.99	44.95